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Nos. 79-374 and 79-386

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1979

BIRMINGHAM TRUST NATIONAL BANK, et al,
Petitioner,

v.

JACK H. HARRISON, et al,
Respondent

JACK H. HARRISON,
Petitioner,

v.

BIRMINGHAM TRUST NATIONAL BANK, et al,
Respondent

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF ALABAMA

BRIEF OF JACK H. HARRISON, AS TEMPORARY TRUSTEE OF THE LINN-HENLEY CHARITABLE TRUST IN RESPONSE TO BRIEF OF THE UNITED STATES AS AMICUS CURIAE AND IN RESPONSE TO THE BRIEF OF BIRMINGHAM TRUST NATIONAL BANK

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INDEX

Page

I. Response to Brief of the United States as Amicus Curiae 1

II. Response to Brief of Birmingham Trust National Bank 2

III. Conclusion 7

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Brief of Jack H. Harrison, as Temporary Trustee of the Linn-Henley Charitable Trust in Response to Brief of the United States as Amicus Curiae and in Response to the Brief of Birmingham Trust National Bank

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I.

Response of Jack H. Harrison, as Temporary Trustee of the Linn-Henley Charitable Trust in support of the brief of the United States as Amicus Curiae, as it relates to the petition of BTNB for a Writ of Certiorari to the Supreme Court of Alabama in Cause No. 79-374

We support the view of the United States that the Petition of Birmingham Trust National Bank to review the decision of the Supreme Court of Alabama, which upheld

the judgment of the court below awarding to the Charitable Trust damages for the fraud and breach of fiduciary duty on the part of the bank, is based solely on state law of trusts and does not involve a federal question.

BTNB in its reply seeks to equate its position with that of the bank in *Simmons*. The distinction between that case and the case sub judice is clear. In *Simmons* a dissenting *stockholder* was simply dissatisfied with the amount of the Comptroller's appraisal and sought to set it aside, and obtain a new appraisal which, as BTNB states, he hoped would result in a larger award.

In the present case, however, the judgment in favor of the Trust was not based upon a review or setting aside of the appraisal of the Comptroller of the Currency. It was based entirely upon the fraud and breach of trust perpetrated by a trustee upon the beneficiaries of an express charitable trust. Thus, there was no attempt to review or override the appraisal made by the Comptroller of the Currency.

The damages awarded to the Trust flowed solely from the fraud, breach of fiduciary duties, conflict of interest and infidelity to the Trust on the part of BTNB, as corporate co-trustee, and on the principle that a wrongdoing trustee should not be allowed to profit by his wrongs, and that a wronged cestui should be made whole by the wrongdoer. Clearly, the judgment was based entirely upon state law of trusts and no federal question is here involved.

II.

Response of Jack H. Harrison, as Temporary Trustee of the Linn-Henley Charitable Trust, in support of his petition for Writ of Certiorari to the Supreme Court of Alabama in Cause No. 79-386

The brief of the United States makes several erroneous assumptions.

(a) In ¶ 2, Page 8, It Is Stated That Petitioner Harrison Challenges The Reversal Of The Award Of Damages To The Trust For Breach Of Fiduciary Duty Stemming From BTNB's Refusal To Permit The Trust To Bid For Shares At The Public Auction.

This statement is clearly erroneous in the face of the unquestionable contention by Petitioner (Petitioner's Petition, p. 28) that the Temporary Trustee never advanced this theory, per se. The real contention of Petitioner is set out on p. 29 of his Petition that ". . . this is not the heart of the case, it is simply another circumstance, which, together with the totality of all of the breaches of fiduciary duty and the violations of federal law, which brings into focus the federal questions here involved."

(b) The Next Point Made By The United States Is That The Complaint Cited Allegations Of Violations Of Federal Law Merely As Examples Of BTNB's Breach Of Fiduciary Duty Under State Law, And That These Violations Were Not Raised ". . . As Separate Federal Causes Of Action That The Alabama Supreme Court Was Required To Adjudicate . . ."

In the first place, the factual statement is incorrect. Under no circumstances can a fair reading of the first five paragraphs of Petitioner's Countercomplaint (A-72-79), of Count II (Pet. p. 32), and the analysis of Claim Two (App. A-82) justify the conclusion that the federal law violations were not raised as separate federal causes of action, nor is there any rhyme or reason to justify the further conclusion that the Alabama Supreme Court was not required to adjudicate the federal law violations apart from the state law question of breach of fiduciary duty. (See, Petition, pp. 28-30).

Furthermore, to follow the argument of the United States to its logical conclusion, it stands for the proposition

that any fraud by a national bank in connection with the purchase or sale of a security which falls clearly within the ambit of 15 U.S.C.A. § 77q(a) and Rule 10b-5, but which is alleged in a complaint as constituting also a violation of a fiduciary duty under state law does not present a federal question. This would pay homage to form rather than to substance, a concept entirely foreign to the Federal Rules of Civil Procedure. It is, of course, the substance of a claim and not the language used in stating it that controls the determination of its nature. *Blitz v. Boog*, 328 F.2d 596, (C.A. N.Y. 1964), Cert. denied, 85 S.Ct. 106, 379 U.S. 855, 13 L.Ed.2d 58.

More importantly, the rationale so advanced by the United States runs counter to the decisions of this and other courts as pointed out on pp. 24-25 of the Petition for Certiorari filed by the Petitioner.

(c) The Brief Of The United States Further Erroneously Seeks To Advance The View That The Comptroller Of The Currency Approved The Triangular Merger Here Involved And That Such Approval Was Entirely Proper On The Basis Of The Literal Terms Of The Banking Act.

In the first place, the record in this case is clear to the conclusion that the Comptroller of the Currency approved only the merger of BTNB into the phantom bank. The record is devoid of any evidence that the Comptroller approved the triangular merger. Indeed, there is nothing in the Banking Act which would permit the Comptroller of the Currency to do so.

On the contrary, as we have shown (Pet. p. 22), § 215a(a) specifically limits mergers to national banking associations and state banks into a national banking association.

Section 215a(d) provides for the sale at public auction of the shares of stock of the "receiving association" which

would have been delivered to the dissenting shareholders had they not requested payment. This is completely inconsistent with the concept that a merger agreement can provide for the delivery of stock of any corporation other than the stock of the "receiving association," especially the stock of a non-banking corporation which cannot be a third member of a triangular merger involving two national banks.

Furthermore, the implication in the brief of the United States that the Comptroller's interpretation of the statute was well established so as to permit triangular mergers in the year 1968 is inconsistent with the policy of the Comptroller as set out in Appendix to this brief.

At any rate, no interpretation of the Comptroller can override the clear provisions of the Federal Banking Act.

Accordingly, and contrary to the contention of BTNB, the failure of the merger agreement and the proxy material to inform the Trust of its right to retain the stock of the "receiving association" in lieu of the stock of the "Holding Company" constituted a material omission of fact, as a matter of law.

(d) In Note 7, Page 9, The United States Indicates That The Petitioner Is Challenging The Merger And Raises The Spectre Of Laches.

In the first place, the countercomplaint disclaims any attempt to unscramble the merger per se.

Secondly, we are dealing here with fraud on the part of a trustee of an express trust to which neither laches nor statute of limitations are applicable under Alabama law. *Heflin v. Heflin*, 93 So. 719, 208 Ala. 69. Furthermore, it is BTNB which filed the proceedings on October 6, 1971 seeking approval of the sale held in 1970. It is the 1970 sale of the "Holding Company" stock at public auction in violation of the Federal Securities laws, and the Regulations

of the Comptroller of the Currency, all accompanied by fraudulent manipulation, which was challenged by the Trust in 1971 and continuously thereafter. To say that such challenge might well be barred by laches is completely unfounded.

Furthermore, no act of the individual co-trustee can give comfort to the joint corporate co-trustee as against the beneficiaries of the Trust represented by Petitioner. There is no privity "between beneficiaries of a trust and the trustee which will make an estoppel against the trustee (Henley) operative against the beneficiaries." 31 C.J.S. Estoppel, § 135, *Fouke v. Schwenewerk*, 197 F.2d 234 (5th Cir.).

The Temporary Trustee is an officer of the court who replaced both trustees for the retrial of this cause. It is the interest of the beneficiaries of the Trust which is to be subserved by the judgments rendered by the court below, and not Henley.

(e) Finally, The United States Concludes That It Does Not Believe That The Petitioner's Federal Securities Law Claims Raised Questions Of Sufficient Importance To Merit Review By This Court.

This conclusion is unwarranted and is not supportable by the facts and the important substantial federal questions, here involved. We entertain the hope that this court deemed the federal questions raised to be of sufficient importance to invite the views of the United States. The United States has shown nothing to justify its belief that the Federal claims raised do not present substantial federal questions of sufficient importance to merit review by this court.

On the other hand, the poor, the hungry and other beneficiaries of this Charitable Trust are silent Petitioners herein to whom the judgment of $1,200,000 based upon federal

law is of the greatest importance. The reversal of this large judgment by the Supreme Court of Alabama clearly denies to them a right under the laws of the United States and merits the consideration and review by this Honorable Court.

III.

CONCLUSION

It follows, therefore, that the petition of BTNB for a Writ of Certiorari to the Supreme Court of Alabama should be denied and that the petition of Jack H. Harrison, as Temporary Trustee of the Linn-Henley Charitable Trust for a Writ of Certiorari to the Supreme Court of Alabama should be granted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Morris K. Sirote, attorney for Jack H. Harrison, as Temporary Trustee of the Linn-Henley Charitable Trust, Respondent herein, and a member of the Bar of the Supreme Court of the United States, do hereby certify that on the day of February, 1980, I served copies of the above and foregoing brief in opposition to the Petition for Writ of Certiorari to the Supreme Court of Alabama, by mailing and depositing same in a United States Post Office or mail box, with first class postage prepaid, in a duly addressed envelope, to Hon. MacBeth Wagnon, Jr., 1500 Brown-Marx Building, Birmingham, Alabama 35203, attorney for Petitioner, Birmingham Trust National Bank; to Hon. Wade H. McCree, Jr., Solicitor General; Hon. Alice Daniel, Assistant Attorney General; Hon. Anthony J. Steinmeyer and Hon. Howard S. Scher, Attorneys, Department of Justice; and to Hon. Ronald R. Glancz and Hon. Ford Barrett, Attorneys, Comptroller of the Currency.

It is further certified that all parties required to be served have been served.

This, the 19 day of February, 1980.

MORRIS K. SIROTE, *Attorney for Jack H. Harrison, as Temporary Trustee of the Linn-Henley Charitable Trust, Respondent*
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APPENDIX

Comptroller of the Currency
Administrator of National Banks
Washington, D. C. 20219

August 22, 1978

Mr. John C. Henley, III
Individual Trustee
The Linn-Henley Trust
Birmingham, Alabama 35203

Dear Mr. Henley:

Your letter of June 5, 1978 to Mr. George LeMaistre, Chairman of the FDIC, regarding the use of "phantom" or "interim" banks to freeze out minority shareholders of national banks, has been referred to this Agency for reply. This Agency has the primary regulatory responsibility for the activities of national banks and their affiliates.

You state in your letter that "the 100% ownership of national banks by holding companies by means of which shareholders in national banks are squeezed out of their national bank stock contrary to law, creates", in your view, "the most serious risks for the future security of the National Banking System".

As you no doubt know, national banks are permitted by statute to merge provided that two-thirds of the shareholders of each association vote in the affirmative. 12 U.S.C. 215a. Section 215a provides further that any shareholder of the target bank who has voted against the merger is entitled to appraisal rights and cash for his or her interest. 12 U.S.C. 215a(b). This reflects the traditional, common law view that an appraisal and payment for one's shares affords fair and just compensation to dissenting sharehold-

ers while allowing the overwhelming majority to proceed with the merger.

Although it has traditionally been the policy of the Comptroller to charter "phantom" or "interim" banks for the purpose of facilitating the acquisition of banks by holding companies, the Comptroller, prior to 1974, did not approve the chartering of these banks for the purpose of facilitating freeze out mergers. Holding companies which were interested in engaging in a corporate reorganization of this type were advised to use the exchange or tender offer process. However, in 1974, it became apparent to the Comptroller that there may be legitimate corporate planning reasons for a holding company to engage in this type of corporate reorganization. Consequently, starting in late 1974, the Comptroller commenced the chartering of "phantom" or "interim" banks, thereby providing the necessary vehicle for the freeze out merger. As a condition precedent to the chartering of these "phantom" or "interim" banks, the Comptroller required a showing of:

(a) a valid business purpose for the merger — that it was not *solely* for the purpose of eliminating minority shareholders;

(b) complete fairness to the minority shareholders — the primary factor being the nature and adequacy of the consideration offered to the minority for their interest; and

(c) an affirmative vote of two-thirds of the minority shareholders.

These requirements were imposed in part because the Comptroller believed — and still believes — that the management, directors and controlling shareholders of a holding company owe a fiduciary obligation of honesty, loyalty, good faith, and fairness to the minority shareholders of affiliated banks and that this fiduciary obligation cannot be fulfilled merely by delegating to the minority shareholders their statutory appraisal rights.

The staff of this Agency is presently engaged in a full scale review of the policy surrounding the "phantom" or "interim" bank chartering process with an eye toward the issuance of a Policy Statement. As part of this review, our staff is in the process of reviewing the case cited in your letter, *Harrison v. Birmingham Trust National Bank*, ... Ala. ....., ... So.2d ..... (Case No. 168-659, Cir. Ct. 10th Cir., 1977), a copy of which was forwarded to us by Macbeth Wagnon, Esq. We would greatly appreciate receiving from you the article prepared by Prof. Loss, as well as any other materials you may have.

I appreciate your concern in this area and trust that this has been responsive to your inquiry.

Very truly yours,

/s/ Roberta Walsh Boylan

Roberta Walsh Boylan
Assistant Director
Legal Advisory Services Division